

General Information Letter: Base income of an individual is federal adjusted gross income, with statutory modifications. No modification requires the add-back of amounts excluded from gross income under cafeteria plans or 401(k) plans, and so such amounts are automatically excluded from base income.

July 20, 2001

Dear:

This is in response to your letter received July 18, 2001 in which you state the following:

We are now offering a 125 Cafeteria Plan (xxxxx) to our employees. Are the pretax dollars under this plan taxable in the State of Illinois? It is our understanding that the pretax dollars deferred by an employee for the company 401(k) plan (xxxxxxxxxxxxx) are not taxable in your state and we would like confirmation of this also.

Are these sums to be included on line 1 of form IL-941?

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill. Adm. Code §1200, or on our website at <http://www.revenue.state.il.us/legalinformation/regs/part1200>. A copy of 2 Ill. Adm. Code §1200 is enclosed for your general information.

Although you have not specifically requested either type of ruling on behalf of your company, the nature of your question and the information provided require that we respond with a General Information Letter. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

Determination of net income for Illinois income tax purposes begins with federal adjusted gross income ("AGI"). Accordingly, any sum properly excluded or deducted from income for federal purposes prior to the determination of AGI is effectively excluded from income for Illinois' purposes. Section 203 of the Illinois Income Tax Act ("IITA") adds back certain amounts of income to federal AGI, but the modifications to AGI described in Section 203 do not include modifications for contributions to a Section 125 Cafeteria Plan or contributions to a 401(k) Plan.

Salary deferrals to Cafeteria Plans authorized under IRC §125 are not part of federal adjusted gross income, and are not added back in determining Illinois base income, therefore such deferrals are exempt from Illinois income tax (i.e., state income tax treatment is the same as federal income tax treatment).

Amounts spent for nontaxable benefits provided under a Section 125 Cafeteria Plan are also exempt from the Illinois income tax. For example, where an employee elects to reduce her salary and accept a group health plan premium paid by her employer in lieu of salary, such premium payment will be exempt from Illinois income tax.

Sums contributed to a Section 401(k) Plan in the form of before-tax salary deferrals are not part of federal adjusted gross income in the year of the deferral and are not added back in determining Illinois base income subject to Illinois income taxation.

Your final question was regarding whether salary deferrals to Section 125 Cafeteria Plans, nontaxable benefits provided under Section 125 Cafeteria Plans and sums contributed to Section 401(k) Plans are to be included on Line 1 of form IL-941.

Illinois income tax regulations Section 100.7030(c) states:

Withholding will not be required under [Section 701 of the IITA] on any payment to the extent such payment is not includable in the recipient's base income.

As discussed above, the base income of an individual is equal to his or her federal adjusted gross income, as modified by Section 203 of the IITA. Salary deferrals to Section 125 Cafeteria Plans, nontaxable benefits provided under a Section 125 Cafeteria Plan and sums contributed to a Section 401(k) Plan are not includable in an individual's federal adjusted gross income and do not cause a modification of such federal adjusted gross income under Section 203. Therefore, such deferrals, benefits and contributions do not need to be included on Line 1 of form IL-941.

As stated above, this is a general information letter which does not constitute a statement of policy that either applies, interprets or prescribes tax law. It is not binding on the Department. Should you have additional questions, please do not hesitate to contact our office.

Sincerely,

Matthew S. Crain  
Staff Attorney -- Income Tax